

PIZZA HUT, INC., ANNUAL REPORT 1973

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BUSINESS
CORPORATION



PIZZA 1000

Opened our 1000th Hut,
Listed: New York Stock Exchange

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Annual Meeting

The Annual Meeting of Shareholders will be held at 9:00 A. M., Monday, August 13, 1973, at the Corporate Offices, Wichita, Kansas. A formal notice of the meeting, together with proxy material, is being sent separately to shareholders.

Corporate Data

Common Stock
Stock symbol: PIZ — Traded NYSE
Transfer Agents: First National City Bank, New York City, and First National Bank in Wichita
Registrars: First National City Bank, New York City, and The Fourth National Bank & Trust Co., Wichita

Auditors

Ernst & Ernst
Wichita, Kansas

Corporate Offices

10225 E. Kellogg
Wichita, Kansas 67207
Tel: (316) 687-4111
For additional information:
A. Tracy Burton
Corporate Information

15 Eventful Years

1958

First Pizza Hut opens. Founded by Dan and Frank Carney, John Bender.

1959

Pizza Hut incorporated in Kansas. First franchise outlet opens in Topeka, Kansas.

1963

Pizza Hut, Inc., adopts standard architectural design for all Huts.

1965-67

Franchise groups show strong growth as multiple operations are developed.

1968

PHI acquires capital stock of 129 franchise corporations.

1969

After meeting SEC requirements, the Corporation offers 410,000 shares of common stock to the public. • Acquires Taco Kid, Next Door, and Flaming Steer restaurant operations. • Expands marketing and distribution capabilities by acquiring two supply companies — Franchise Services, Inc., and J&G Food Co., Inc. • Opens additional Huts in Canada and Mexico.

1970

New international headquarters at 10225 East Kellogg in Wichita observes formal opening with Governor Robert B. Docking of Kansas in attendance. This modern facility on a 20-acre site houses primary offices for all divisions and subsidiaries, including research and development center and electronic data processing center. • PHI opens first two units overseas — in Munich, Germany, and Sydney, Australia. • Announces formation of Sunflower Food Processors, Inc., as a joint venture with Sunflower Beef, Inc.

1972

1000th Pizza Hut opened. • PHI is listed on the New York Stock Exchange November 30 under the symbol PIZ. Pizza Hut's largest franchisee, Pizza Corporation of America, becomes a public company, listed on the American Stock Exchange November 15 under the symbol PZA.

Highlights

	1973	1972 (Restated)
Total Revenue	\$66,924,439	\$48,562,443
Net Income	\$ 3,505,394	\$ 2,130,795
Per Share Income	\$ 1.10	.73
Working Capital	\$ 5,858,360	\$ 1,938,847
Total Assets	\$36,194,233	\$24,570,584
Stockholders' Equity	\$22,686,144	\$12,822,345

Quarterly Review

	1973			1972 (Restated)		
	Sales	Net Income	Earnings Per Share	Sales	Net Income	Earnings Per Share
FIRST QUARTER Ended June 30	\$14,201,943	\$ 801,141	\$.27	\$ 9,687,809	\$ 432,973	\$.15
SECOND QUARTER Ended Sept. 30	\$16,025,902	\$ 891,221	\$.28	\$11,480,456	\$ 571,145	\$.20
THIRD QUARTER Ended Dec. 31	\$16,795,986	\$ 944,427	\$.29	\$12,608,898	\$ 588,759	\$.20
FOURTH QUARTER Ended March 31	\$17,429,388	\$ 868,605	\$.26	\$13,253,405	\$ 537,918	\$.18
TOTAL	\$64,453,219	\$3,505,394	\$1.10	\$47,030,568	\$2,130,795	\$.73

Corporate Growth Trends Years Ended March 31
(All prior years restated)



In November, 1972, Pizza Hut celebrated the opening of its 1000th Pizza Hut with an informal ceremony in Wichita that included Federal, state, and local dignitaries. It was also in 1972 that Pizza Hut took the lead in retail sales in the fast food pizza field. A good product, sound management, and a workable plan all helped Pizza Hut to reach this goal. The opening of the 1000th Hut was an excellent symbol of this accomplishment.

Joining together for the 1000th Hut opening were, left to right, U.S. Senator James B. Pearson of Kansas, Dan and Frank Carney, and Kansas Attorney-General Vern Miller.



Five Year Pizza Hut Growth

At March 31,	1969	1970	1971	1972	1973
Total Units — Pizza Huts	330	522	668	855	1129
Company Units Open	149	218	259	359	490
Franchise Units Open	181	304	409	496	639
Average Co. Annual Sales Per Unit	\$98,175	\$101,975	\$103,030	\$112,567	\$124,686

Units Under Construction or Leases Signed

Company	42	59
Franchised	71	106



Report to the Stockholders

Pizza Hut, Inc.'s fiscal 1973 plan was well executed by your management team. We responded to the challenges of fast growth, increased and changing governmental control guidelines with a record year in all categories.

Sales, net income, and earnings per share increased sharply as shown in this report. In this letter I want to (1) focus attention on significant events of fiscal 1973, (2) acquaint you with the key challenges that confront our management team, and (3) describe to you our plan for fiscal 1974.

Significant events . . . Fiscal '73 (April 1, 1972 through March 31, 1973) was a great year for establishing benchmarks of maturity.

- Opened 1000th Pizza Hut November 2, 1972.
- Opened largest number of units in one year . . . 276
- Pizza Hut, Inc. was listed on the New York Stock Exchange on November 30, 1972 . . . Symbol PIZ
- Opened a second distribution center in Peoria, Illinois. We are now servicing over 500 Pizza Huts with direct weekly deliveries.
- Our largest franchisee, Pizza Corporation of America, was listed on the American Stock Exchange . . . Symbol PZA
- Introduced the new 15" pizza in Pizza Huts.
- Added the experience of Louis Pozez and King Shwayder to our Board of Directors.

Key Challenges . . . Growth is synonymous with change, and we as management must meet the challenges of constant change. The following summarizes the major challenges and your management's responses to those challenges.

Financing Our Continued Growth
A \$6,250,000 public offering in August of 1972 expanded the capital base of the Company. During fiscal year 1973, we negotiated the private sale of \$6,000,000 of Senior Notes and made the first of three \$2,000,000 draws in April of 1973. We have negotiated the major terms of \$7,000,000 in sale-leasebacks. The above financing and sale-leasebacks coupled with our cash flow and normal build-to-suit transactions should insure the financing of our growth through fiscal 1975.

To Increase Sales and Productivity In Our Pizza Units
We established a cooperative advertising program between

company and franchise units within geographical television markets, thus increasing the effectiveness and efficiency of our advertising dollars while complementing our national program.

We have directed the efforts of Marketing, Research & Development, and Training to test programs that will better insure the success of new products, advertising, and operating procedures designed for the Pizza Divisions.

Unprofitable Units in California And Their Impact On Corporate Earnings

We have strengthened the operational management in the California market and have cut the monthly loss in half. Management is dedicated to achieve a turnaround in fiscal year 1974.

Equitable Compensation and Profit Sharing

We have revised the compensation system and instituted an improved fringe benefit package, including improved insurance, employee profit sharing plan, and a monthly investment plan for Pizza Hut stock administered through a major brokerage firm so that employees can share in the growth and ownership of the Company.

Restaurant Division: Next Door, Taco Kid, Fiesta Cantina, And Flaming Steer

The operating losses from the Restaurant Division have been eliminated. Our goal is to optimize the profitability of the operating units and continue to build a capable management team.

Excess Properties

Management's policy is that all properties not used by Pizza Hut, Inc. operations or subsidiaries are classified "Excess." These properties include closed operational units and/or adjacent land to existing operational units and some undeveloped commercial property. Our Property Management Division will continue the proven method of subleasing properties to other users and, when possible, exercise opportunities to buy out leases to eliminate contingent liabilities.

Corporate Office Overhead

We have instituted a planned decrease of corporate overhead each year in relation to sales. With the completion of all departments necessary to support the operations, a commitment for a percentage decrease has been made an integral part of all management goals.

Ready Italy

This frozen pizza crust manufacturing company was acquired by Pizza Hut, Inc. in December, 1970. All products from Ready Italy were sold to outside frozen food companies and were not used in Pizza Hut operations. The sale of this company was completed May 31, 1973.

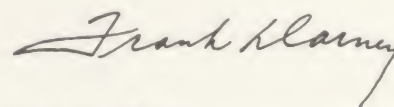
Our plans have emphasized the concentration of efforts on pizza operations, both domestic and foreign, and Ready Italy was not a part of the vertical support system designed to insure the success of the Pizza Division. This will not affect our research and testing of frozen products or other complementary food items which were being considered for the Pizza Division.

Plan for Fiscal '74 . . . Our plans are overwhelmingly directed towards the Pizza Division and its necessary support systems.

- We plan to build 100 more company units in addition to the 180 contemplated by franchisees.
- We have announced the April, 1973, acquisition of 23 franchise units.
- Within the next twelve months we will add the franchisee-proven spaghetti program to company units.
- Our International Division will open the first Pizza Huts in England and Japan and continue to expand in Australia, Canada, Mexico and Germany. Our plan in the International area is purposely slow paced, with initial penetration of new areas and consistent profitable expansion in existing areas. Our International Division will not be a significant contributor to Pizza Hut earnings in the next few years but later could grow to match the profitability of the U.S. operations.

With this information, and a thorough study of this report, you will have a current, accurate picture of Pizza Hut, Inc. We are meeting our primary goal of consistent growth in earnings per share, both short and long term. We are proud of our experienced management team and appreciate your continued support.

Respectfully,



Frank L. Carney
President and Chairman of the Board



**Fiscal Year Ended March 31
(Dollars in Thousands)**

	1969*		1970*		1971*		1972*		1973	
	\$	%	\$	%	\$	%	\$	%	\$	%
Revenues:										
Company operated Pizza Huts	13,816	92.9	21,099	82.3	26,943	77.9	38,174	78.6	52,044	77.8
Product sales to franchisees	308	2.1	2,402	9.4	3,080	8.9	4,820	9.9	8,367	12.5
Other restaurants	305	2.1	1,116	4.4	2,879	8.3	3,663	7.5	3,761	5.6
Frozen pizza pie crusts					411	1.2	373	.8	281	.4
Franchise fees:										
Initial	170	1.1	476	1.8	386	1.1	462	1.0	726	1.1
Continuing	280	1.8	545	2.1	874	2.6	1,070	2.2	1,745	2.6
	14,879	100.0	25,638	100.0	34,573	100.0	48,562	100.0	66,924	100.0
	*Restated									

The development, operation, franchising, and servicing of Pizza Huts, which are casual family restaurants serving Italian food primarily for consumption on the premises, is the principal business of Pizza Hut, Inc. A limited number of Mexican food, specialty, and steak restaurants are also operated by the company. In addition Pizza Hut, Inc. manufactures certain fixtures and supplies, processes certain pizza ingredients, and

purchases, warehouses, and distributes equipment, supplies, and food products for use in its Pizza Hut restaurant operations, and sale to franchisees. Pizza Hut, Inc. recently sold its interest in Ready Italy, Inc., a manufacturer of frozen pizza pie crusts. The frozen crusts were not used in Pizza Huts but were sold to frozen pizza pie manufacturers.



**Fiscal Year Ended March 31
(Dollars in Thousands)**

	1969*		1970*		1971*		1972*		1973	
	\$	%	\$	%	\$	%	\$	%	\$	%
Contribution to Income:										
Company operated Pizza Huts	2,159	82.3	2,291	64.8	3,883	86.1	6,100	87.6	8,241	79.0
Product sales to franchisees	24	.9	331	9.4	98	2.2	401	5.7	614	5.9
Other restaurants & excess property costs	(10)	(.4)	(109)	(3.1)	(745)	(16.5)	(995)	(14.3)	(631)	(6.0)
Frozen pizza pie crusts					16	.3	(72)	(1.0)	(261)	(2.5)
Franchise fees:										
Initial	170	6.5	476	13.5	386	8.6	462	6.6	726	6.9
Continuing	280	10.7	545	15.4	874	19.3	1,070	15.4	1,745	16.7
	<u>2,623</u>	<u>100.0</u>	<u>3,534</u>	<u>100.0</u>	<u>4,512</u>	<u>100.0</u>	<u>6,966</u>	<u>100.0</u>	<u>10,434</u>	<u>100.0</u>
	*Restated									

Each activity is shown in these tables by the respective amounts and percentages of revenues and by contributions to consolidated income before general and administrative expenses attributable to the home office, interest expense, and income tax.

Pizza Hut, Inc. believes that allocating such expenses, interest, and taxes would be arbitrary due to the close relationship and interdependency of all company activities. Expenses (other than general and

administrative expenses attributable to the home office, interest expense, and income taxes) related to "franchise fees" have been allocated to "Company-operated Pizza Huts."

The above table includes the sales by businesses acquired by the Company for all periods since March 31, 1968 in transactions accounted for as poolings of interest and eliminates intercompany transactions.

Pizza Hut, Inc. Operating Divisions

Pizza Hut Operations

Fiscal '73 saw 276 new Huts begin operations, making a total of 1,129 retail stores. Ninety-nine Huts were under construction at the close of fiscal '73, one-third company owned. Leases were signed on an additional 66 units, 26 of these company owned and 40 franchised.

Unit expansion and comparable unit sales increases stayed on target. The annual volume of business at Pizza Huts now averages \$125,000, compared with \$112,500 last year.

Formal management training has been strongly emphasized during this fiscal year. Management has found this to be very effective, both for the individual and the company, resulting in better efficiency and length of tenure — with a 91.8% retention rate for employees who have attended the training schools. Fiscal '74 will include additional sessions and expansion of the field training program, using the PHI-developed audio-visual training package.

The Company plans to place this training aid in every store and to develop at least six new audio-visual programs in the coming year.

Franchise Services, Inc.

Every week twenty-one refrigerated and seven dry trailers transport food, supplies, frozen products, and equipment from two warehouses in Wichita, Kansas and one in Peoria, Illinois, to 575 Pizza Huts. These Huts have a convenient, competitively priced source of supply while keeping only minimum inventory.

The Peoria distribution center opened during fiscal '73. Other distribution centers are planned for later development.

FSI employs 100 people and utilizes computerized warehouse and accounting systems. Inventory is \$1.5 million. Annual volume is more than \$16 million.



(Approximately \$8 million of these sales are to company units; therefore, annual consolidated figures of PHI sales reflect only \$8.5 million.)

Franchise Services, Inc. also carries food and supplies for the Taco Kid-Fiesta Cantina Division and for three other taco chains unrelated to Pizza Hut, Inc. In addition, other specialty items are inventoried for the Next Door and Flaming Steer Divisions.

J&G Products, Inc.

This company was originally established as a manufacturing firm to produce specialty goods which were difficult to obtain. Today, J&G manufactures both specialty and standard line items used by Pizza Hut retail operations.

J&G contributes to the profitability of Pizza Hut by providing quality items at competitive prices.

Flaming Steer

Two company-owned Flaming Steer restaurants feature steak, seafood, and chicken dinners at moderate prices. They also offer hostess seating and full table service. Decor is Spanish Mediterranean. Bum steer, a supper club in the same building, shares connecting kitchen facilities for increased profitability. Average volume of each unit exceeds \$700,000 per year.

Next Door

There are five company-owned Next Door restaurant operations. Early American decor is used throughout, accented by bright reds and blues in furniture and carpeting. The menu includes steaks, specialty foods, seafood, as well as hamburgers, sandwiches, salads, soft drinks, and desserts.

Taco Kid — Fiesta Cantina

Adjustments were made to the Taco program and existing operations were remodeled, featuring a rustic Spanish decor, emphasizing full dine-in facilities with a complete selection of Mexican dinners. Two previously closed units have been reopened. There are now 12 company-owned stores. Average volumes per unit: Taco Kid, \$90,000; Fiesta Cantina, \$110,000.





Pizza Hut International Operations

Pizza Hut pizza is fast becoming an international food. Foreign operations have grown successfully and are expected to be greatly expanded in the coming years.

Forty-seven company-owned and franchised Pizza Huts are now operating in Mexico, Canada, Costa Rica, Australia, West Germany, and England. Six are under construction and two others have developed to the lease-signing stage. About half are company-owned and half franchised units. Inquiries for franchising have been received from many countries throughout the world.

A joint venture between Pizza Hut, Inc. and Sumitomo Shoji Kaisha, Ltd. has resulted in the formation of Pizza Hut Japan, Ltd., which expects to open its first Hut in fiscal 1974.

Australia, followed by Canada, leads in Hut activity, both in number of operating units and in total volume of sales.

The pizza served in the foreign Huts is the same basic product as served in the U.S.A. — thin crust, spicy sauce, mild cheese, and lots of topping. The most noticeable difference in the product is its presentation, especially in Germany. To match the expected dining atmosphere more nearly, the Pizza Hut menu often includes a full wine list.

The Operations Manual has been translated into German, Spanish, and soon will be translated into Japanese. Pizza Hut International furnishes management personnel to assist in each country; however, all employees are hired from the local community.





Left to right: Daniel M. Carney, Investments, Frank L. Carney, Chairman of the Board and President
 Martin T. Hart, Investments, King D. Shwayder, President, Samsonite Corporation
 James P. Schwartz, Vice President, Finance (deceased, June 16, 1973)
 Louis Pozez, President, Volume Shoe Corporation
 G. E. Engleman, Chairman of the Board, Union Bank of Ft. Worth and First National Bank, Hurst, Texas



Frank L. Carney
 President and Chairman of the Board



Robert E. Cressler
 Group Vice President, Operations



James P. Schwartz
 Vice President, Finance
 (deceased, June 16, 1973)

Board of Directors and Principal Officers

Gerald T. Aaron
Secretary and Counsel

Farris S. Farha
Vice President,
Administration



Robert L. Logsden
Vice President,
Marketing and Research

Kenneth R. Miller
Vice President,
Pizza Operations



Larry F. Payne
Vice President,
Restaurant Division

John H. Songer
Vice President,
Property Management



Daniel J. Taylor
Treasurer and
Chief Accounting Officer

M. Hal Taylor, PhD
Vice President,
Distribution and
Food Processing





The I.P.H.F.H.A. is scheduling more than 250 Pizza Hut TV commercials on all major TV networks.

Just as the national advertising program has grown, so have the advertising efforts of I.P.H.F.H.A. involvement in Pizza Hut's local markets. The Association has worked closely with the Marketing Department in developing the Pizza Hut ADI program (area of dominant influence).

The I.P.H.F.H.A. Board of Directors and the regions they represent are:

Jamie Coulter, Southeast,
President

Gerry MacNeil, Eastern

Howard Wilkins, Western

Dave Remmert, Midwest

George Middleton, Central

Virgil Boll, Southwest

Sam Moyers, representative
Pizza Hut, Inc.

Dan Hesse,

Association Director

Michael L. Stegman,

Association Administrator

Pizza Hut Basketball Classic

The Second Annual Pizza Hut Basketball Classic was held April 14 in Las Vegas Convention Center. An independent network televised it to 130 stations and millions viewed the game.

Balloting to choose the players had taken place from early January to mid-March in all of Pizza Hut's domestic outlets and through 100 participating universities. This year the players were chosen by 800,000 votes.

Through the Classic, selected charitable organizations throughout the country receive substantial donations to continue their specific work. This year donations were contributed to

- Foundation for Research and Education in Sickle Cell Disease
- Continuing Education Fund of National Association of Collegiate Directors of Athletics
- Basketball Congress of America — Boys Division
- University of Nevada, Las Vegas - Building Fund.

In addition, a small donation was made to the U.S. Basketball Writers Association for publication of their annual directory.



Franchising 1973

Operational ownership that accelerates PHI growth.

The franchise industry is coming into its own as a dominant force in the economy of our country. More than 420,000 franchise outlets generate over \$140 billion in sales each year in the United States. That figure equals approximately 25% of total annual retail sales in the United States.

The aggressive Pizza Hut franchise organization is one of the most successful in the world. The franchisees, a diverse group of independent business people, have accelerated the growth of Pizza Hut, Inc. They have access to PHI management know-how and bring a total commitment to company goals but, at the same time, maintain operational control and ownership in each of their individual units.

The typical franchisee is a multiple unit operator. The ten largest franchise groups operate over 300 units. Less than 25 of the franchise units are singly owned and operated.

More than 90% of the franchisees attended the 1973 Annual Franchise Meeting held in San Diego in January. This meeting provided them with additional ideas about advertising, effective and profitable Hut operations, and staff motivation and management.

A major benefit of the annual meeting is the opportunity to get better acquainted with each other and exchange practical ideas relating to special needs and interests of the franchisee.

Other communications with the franchise organization include quarterly meetings of the Franchise Advisory Board (whose function it is to review company policies and programs) and the quarterly visits by company personnel to each franchise unit.



Statements of Consolidated Income

Pizza Hut, Inc. and Subsidiaries

	Years Ended March 31,		
	1973	1972	
		As Restated — Note B	As Previously Reported
Net sales.....	\$64,453,219	\$47,030,568	\$42,872,758
Cost of sales.....	22,569,520	16,085,314	14,890,677
	41,883,699	30,945,254	27,982,081
Initial franchise fees.....	726,000	462,000	502,000
Continuing franchise fees.....	1,745,220	1,069,875	1,184,292
Equity in net income of unconsolidated foreign subsidiaries and minority owned affiliates.....	151,436	113,824	158,989
	44,506,355	32,590,953	29,827,362
Selling, general, and administrative expenses.....	37,640,987	28,342,733	25,973,324
	6,865,368	4,248,220	3,854,038
Other income (including interest: 1973 — \$364,741; 1972 — \$127,610).....	507,737	280,245	270,388
	7,373,105	4,528,465	4,124,426
Interest expense.....	634,299	424,828	392,776
INCOME BEFORE INCOME TAXES.....	6,738,806	4,103,637	3,731,650
Federal and state income taxes:			
Currently payable.....	3,448,412	1,854,842	1,719,000
Deferred	(215,000)	118,000	118,000
	3,233,412	1,972,842	1,837,000
NET INCOME.....	\$ 3,505,394	\$ 2,130,795	\$ 1,894,650
Net income per share:			
Primary — assuming exercise of options and warrants.....	\$1.11	\$.74	\$.75
Fully diluted — assuming, in addition, conversion of convertible notes.....	\$1.10	\$.73	\$.74

See notes to consolidated financial statements.

Consolidated Balance Sheets

Pizza Hut, Inc. and Subsidiaries

		March 31, 1972	
		As	As
		Restated —	Previously
		Note B	Reported
		March 31, 1973	
ASSETS			
CURRENT ASSETS			
Cash	\$ 2,378,535	\$ 2,461,736	\$ 2,234,591
Certificates of deposit	4,700,000	100,000	100,000
Marketable securities — at cost which approximates market		1,000,000	1,000,000
Receivables:			
Notes	321,787	379,446	379,446
Trade accounts	1,557,035	949,104	949,104
Other accounts — Note D	751,265	190,361	141,558
Allowance for doubtful notes and accounts	(65,000)	(65,000)	(65,000)
	2,565,087	1,453,911	1,405,108
Inventories	2,645,231	1,688,483	1,608,569
Prepaid expenses	301,127	265,286	233,253
TOTAL CURRENT ASSETS	12,589,980	6,969,416	6,581,521
INVESTMENTS AND OTHER ASSETS			
Investments in and advances to unconsolidated affiliates:			
Foreign subsidiaries	1,444,129	609,146	689,569
Other affiliates — Note B	601,408	344,163	344,163
	2,045,537	953,309	1,033,732
Cost in excess of net assets of businesses acquired	1,642,565	1,389,733	1,389,733
Patents, service marks, and franchises	438,257	406,614	406,614
Notes receivable (less allowance of \$50,000) and other accounts	1,472,926	1,289,022	1,187,551
	5,599,285	4,038,678	4,017,630
PROPERTY, PLANT, AND EQUIPMENT — Note C			
Land	3,561,042	2,328,327	2,244,102
Buildings and improvements	2,636,114	1,790,095	1,753,894
Leasehold improvements	4,825,478	3,842,639	3,674,590
Operating equipment	10,337,658	7,179,371	6,652,684
Construction in progress		791,856	791,856
	21,360,292	15,932,288	15,117,126
Allowances for depreciation and amortization (deduction)	(4,355,468)	(3,172,890)	(3,002,982)
	17,004,824	12,759,398	12,114,144
DEFERRED CHARGES			
Organization expense	302,734	359,790	353,654
Deferred income taxes	379,000	164,000	164,000
Other	318,410	279,302	279,302
	1,000,144	803,092	796,956
	<u>\$36,194,233</u>	<u>\$24,570,584</u>	<u>\$23,510,251</u>
LIABILITIES AND STOCKHOLDERS' EQUITY			
CURRENT LIABILITIES			
Notes payable	\$ 21,500	\$ 297,079	\$ 277,138
Trade accounts payable	2,223,219	1,279,900	1,221,355
Taxes, other than income	911,160	739,100	688,486
Federal and state income taxes	2,141,634	1,387,407	1,316,392
Other accrued expenses	647,488	360,594	343,513
Current portion of long-term debt	786,619	966,489	879,449
TOTAL CURRENT LIABILITIES	6,731,620	5,030,569	4,726,333
LONG-TERM DEBT — less portion classified			
as current liability — Note C	5,979,469	6,203,787	5,967,646
DEFERRED INITIAL FRANCHISE FEE INCOME	797,000	513,883	518,383
STOCKHOLDERS' EQUITY — Note E			
Preferred Stock — \$0.01 par value			
Authorized 1,000,000 shares; none issued	—	—	—
Common Stock — \$0.01 par value			
Authorized 10,000,000 shares; issued and outstanding			
3,174,914 shares in 1973 and 2,914,265 shares in 1972	31,749	29,143	25,752
Other capital	362,547	362,547	341,524
Additional paid-in capital	13,851,177	7,495,378	7,191,006
Retained earnings	8,440,671	4,935,277	4,739,607
	22,686,144	12,822,345	12,297,889
COMMITMENTS AND CONTINGENT LIABILITIES — Note F			
	<u>\$36,194,233</u>	<u>\$24,570,584</u>	<u>\$23,510,251</u>

See notes to consolidated financial statements.

Statement of Consolidated Stockholders' Equity

Pizza Hut, Inc. and Subsidiaries

Years ended March 31, 1973 and March 31, 1972

	Common Shares	Stock Amount	Other Capital	Additional Paid-In Capital	Retained Earnings
Balance at April 1, 1971:					
As previously reported.....	2,517,236	\$25,173	\$341,524	\$ 6,369,816	\$2,844,957
Adjustment for acquisition of pooled companies — Note B.....	281,800	2,818		284,170	48,051
As restated.....	2,799,036	27,991	341,524	6,653,986	2,893,008
Acquisition of purchased companies — Note B...	53,846	538		699,459	
Sale of warrants to purchase 52,500 shares — Note C.....				78,750	
Exercise of employee stock options — Note E....	4,088	41		35,904	
Amounts received under employee stock option plan to extend options previously granted.....				7,077	
Acquisition in 1973 of pooled companies formed in 1972 — Note B.....	57,295	573	21,023	2,537	(21,023)
Capital transactions of pooled companies before acquisition.....				17,665	
Dividends declared by pooled companies before acquisition.....					(67,503)
Net income.....					2,130,795
BALANCE AT MARCH 31, 1972.....	2,914,265	29,143	362,547	7,495,378	4,935,277
Acquisition of pooled company formed in 1973 — Note B.....	3,560	36		964	
Exercise of employee stock options — Note E...	4,148	41		37,212	
Amounts received under stock option plan to extend options previously granted.....				4,275	
Sale of warrants to purchase 35,000 shares — Note C.....				78,750	
Sale of Common Stock.....	250,000	2,500		6,209,627	
Conversion of an 8% Convertible Note — Note C.....	2,941	29		24,971	
Net income.....					3,505,394
BALANCE AT MARCH 31, 1973.....	3,174,914	\$31,749	\$362,547	\$13,851,177	\$8,440,671

See notes to consolidated financial statements.

Statements of Changes in Consolidated Financial Position

Pizza Hut, Inc. and Subsidiaries

	Years Ended March 31,		
	1973	1972	
		As Restated — Note B	As Previously Reported
SOURCE OF FUNDS			
Net income	\$ 3,505,394	\$ 2,130,795	\$ 1,894,650
Charges to income not affecting funds:			
Depreciation and amortization	1,556,942	1,644,087	1,551,407
Decrease (increase) in deferred income taxes	(215,000)	118,000	118,000
Equity in net income of unconsolidated foreign subsidiaries and other affiliates	(151,436)	(113,824)	(158,989)
TOTAL FROM OPERATIONS	4,695,900	3,779,058	3,405,068
Proceeds from long-term debt	1,003,364	4,859,197	4,793,464
Disposals of property, plant, and equipment	1,581,247	862,721	796,997
Increase in deferred initial franchise fees	283,117		
Issuance of Common Stock and Common Stock warrants	6,290,877	814,692	814,692
Other items	67,528	7,077	9,460
	<u>13,922,033</u>	<u>10,322,745</u>	<u>9,819,681</u>
APPLICATION OF FUNDS			
Acquisition of assets of businesses purchased:			
Property, plant, and equipment	295,126	1,795,534	1,795,534
Franchise rights and other assets	59,684	378,123	378,123
Cost in excess of net assets acquired	304,059	859,994	859,994
Long-term debt assumed		(345,833)	(345,833)
	<u>658,869</u>	<u>2,687,818</u>	<u>2,687,818</u>
Additions to property, plant, and equipment	6,928,947	3,475,915	3,159,836
Reduction of long-term debt	1,227,682	1,511,419	1,473,639
Investments in and advances to unconsolidated foreign subsidiaries and other affiliates	940,792	564,811	583,759
Other items	246,230	214,147	158,476
	<u>10,002,520</u>	<u>8,454,110</u>	<u>8,063,528</u>
INCREASE IN WORKING CAPITAL	<u>\$ 3,919,513</u>	<u>\$ 1,868,635</u>	<u>\$ 1,756,153</u>
INCREASE (DECREASE) IN WORKING CAPITAL BY COMPONENT			
Cash	(\$ 83,201)	\$ 1,398,605	\$ 1,268,891
Certificates of Deposit and marketable securities	3,600,000	1,100,000	1,100,000
Trade and other receivables	1,111,176	(572,949)	(609,075)
Inventories	956,748	471,676	440,092
Prepaid expenses	35,841	9,399	2,629
Notes payable and current portion of long-term debt	455,449	861,396	908,728
Trade accounts payable and accrued expenses	(1,402,273)	(581,253)	(557,715)
Income taxes	(754,227)	(818,239)	(797,397)
INCREASE IN WORKING CAPITAL	<u>\$ 3,919,513</u>	<u>\$ 1,868,635</u>	<u>\$ 1,756,153</u>

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

Pizza Hut, Inc. and Subsidiaries

March 31, 1973 and 1972

NOTE A — ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of all domestic subsidiaries after elimination of significant intercompany accounts and transactions.

FOREIGN SUBSIDIARIES AND OTHER AFFILIATES

Investments in wholly-owned subsidiaries in Australia, Canada, Germany, and Mexico and investments in certain minority owned domestic affiliates are carried at cost plus equity in net income of the foreign subsidiaries and domestic affiliates.

Because the Company plans to continue to finance foreign expansion and operating requirements by re-investment of undistributed earnings of its foreign subsidiaries, United States income taxes have not been provided on such earnings. The amount of undistributed earnings at March 31, 1973 which are considered to be indefinitely reinvested is approximately \$129,000.

INVENTORIES

Inventories are stated at the lower of cost (first-in, first-out method) or market.

PROPERTY, PLANT, AND EQUIPMENT AND DEPRECIATION POLICIES

Property, plant, and equipment is carried on the basis of cost and includes assets carried at \$848,051 which have been acquired under the capitalized lease obligation discussed in Note C.

Depreciation is determined by the straight-line and accelerated methods over the following range of useful lives:

Buildings and improvements	20 to 30 years
Operating equipment	3 to 10 years
Leasehold improvements	Term of lease

AMORTIZATION POLICIES

Amortization of intangibles and deferred charges is determined using principally the straight-line method. The cost in excess of net assets of businesses acquired prior to October 31, 1970 (\$500,929) is not amortized since, in the opinion of management, there has been no diminution in value. Such amounts acquired after October 31, 1970 (\$1,180,315) are amortized over a forty-year life. Franchise rights, deferred debt expense, and organization costs are amortized over fifteen-year lives. Deferred site development costs are amortized over five-year lives.

INITIAL FRANCHISE FEE INCOME

Upon the sale of a franchise, the Company records the amount received or receivable as an asset and the fee as deferred franchise fee income. The initial franchise fee is recorded as income when the retail unit has been opened by the franchisee.

DEFERRED INCOME TAXES

Deferred income taxes arise primarily from the timing difference created by the deferral, for financial statement purposes, of initial franchise fee income as described above while recognizing, for tax purposes, such income currently.

INVESTMENT TAX CREDITS

Investment tax credits, which amounted to \$264,000 in 1973 and \$116,000 in 1972, are accounted for using the flow-through method.

NET INCOME PER SHARE

Employee stock options, warrants attributable to the 8¾% Senior Notes, and options under a director's deferred compensation plan are considered to be Common Stock equivalents in the computation of primary net income per share using the treasury stock method applied at the average market price during the period.

In the computation of fully-diluted net income per share, the Common Stock equivalents plus the shares issuable in the assumed conversion of the 8% convertible notes are considered and interest expense (net of applicable income taxes) attributable to the convertible notes is added to net income. The treasury stock method is applied to Common Stock equivalents at the year end market price if higher than the average market price.

NOTE B — ACQUISITIONS

During 1973, the Company acquired 45 Pizza Hut restaurants, including 7 Canadian restaurants, in exchange for 342,655 shares of the Company's Common Stock in transactions accounted for as poolings of interests. The operations of the acquired units have been included in the financial statements for the entire year of 1973 and the 1972 financial statements have been restated to include these units. Following is a summary of the results of operations of the pooled companies (after elimination of intercompany transactions) included in the accompanying 1973 financial statements for periods prior to the dates of acquisition:

Net sales	\$1,050,730
Equity in net income of unconsolidated foreign subsidiary	5,259
Net income	32,235

In 1972, the Company acquired one Pizza Hut restaurant for 7,583 shares of the Company's Common Stock in a transaction accounted for as a pooling of interests. The 1972 statements of consolidated income include net sales of \$107,823 and net income of \$4,490 of this pooled company prior to the date of its acquisition.

During 1973, the Company also acquired 10 Pizza Hut restaurants in transactions accounted for as purchases. The cost of these units was \$656,374 and this cost exceeded the value of the net assets acquired by \$304,059. In 1972, the Company acquired 36 Pizza Hut restaurants and 15 other pizza restaurants in transactions accounted for as purchases. The cost of these units was \$1,699,013 (including 53,846 shares of the Company's Common Stock valued at \$699,998) and this cost exceeded the value of the net assets acquired by \$859,994. The operations of these units have been included in the accompanying statements of consolidated income from the respective dates of their acquisition. Following are consolidated results of operations of the Company on a pro forma basis assuming that units purchased during 1972 and 1973 had been combined at the beginning of 1972:

	1972		
	1973	Restated For Poolings	As Originally Reported
Net sales	\$65,027,463	\$50,399,007	\$46,241,197
Net income	3,561,141	2,220,425	1,984,280
Net income per share:			
Primary	\$1.13	\$.77	\$.78
Fully diluted ...	1.12	.76	.77

During 1972, the Company purchased wholly-owned, unconsolidated Canadian and Mexican subsidiaries at a cost of \$520,145. This cost exceeded the value of the subsidiaries net assets by \$143,148 and the excess, which is included with the investments in the accompanying balance sheet, is being amortized over a forty-year period using the straight-line method. The Company's equity in the net income of these subsidiaries has been included in the accompanying statements of consolidated income from their respective dates of acquisition; however, the results of operations for periods prior to acquisition, which were

not material, were not included in the above pro forma information.

NOTE C — LONG-TERM DEBT

Following is a summary of long-term debt:

	1972		
	1973	As Restated — Note B	As Previously Reported
8¾% Senior Notes issued with detachable warrants to purchase 87,500 shares of Common Stock at \$9.25 a share. Face value \$2,500,000 (less a discount of \$149,625 attributable to warrants resulting in an effective interest rate of 9½%) payable in annual installments of \$250,000 from March, 1978 to March, 1987	\$2,350,375	\$1,421,250	\$1,421,250
Notes payable to banks in quarterly installments of \$100,000 plus interest at 1¼% over prime rate to December, 1976	1,500,000	1,900,000	1,900,000
Mortgage notes payable in monthly installments of \$14,932, including interest at rates from 6½% to 12% maturing at various dates through 1991. Land, buildings, and leasehold improvements with a carrying value of \$1,856,035 have been mortgaged as collateral	1,078,942	1,474,889	1,374,351
Capitalized lease obligation payable through 1985 in increasing monthly installments including interest from 7½% to 8¾% (See Note G)	925,000	975,000	975,000
Equipment notes payable in monthly installments of \$15,316, including interest at rates of 3% to 10.18%, maturing at various dates through 1979. Equipment with a carrying value of \$514,151 has been mortgaged as collateral ...	220,463	441,629	301,071
8% notes, due in September, 1976, convertible into shares of the Company's Common Stock at the rate of \$8.50 per share	225,000	250,000	250,000

Other unsecured notes payable in monthly installments of \$10,216 plus interest at rates of 3.85% to 10% maturing at various dates through 1977	466,308	707,508	625,423
	<u>6,766,088</u>	<u>7,170,276</u>	<u>6,847,095</u>
Less amounts due within one year	786,619	966,489	879,449
	<u>\$5,979,469</u>	<u>\$6,203,787</u>	<u>\$5,967,646</u>

The Company has agreed, under certain long-term debt agreements, to maintain working capital of \$1,200,000 and to maintain a current ratio of at least 1.5 to 1. The agreements also contain certain restrictions which, among other things, prohibit the payment of dividends unless certain earnings and debt service tests are met. At March 31, 1973, the Company did not satisfy the conditions necessary to allow the payment of dividends.

Maturities of long-term debt for the next five years are as follows: 1974 — \$786,619; 1975 — \$730,370; 1976 — \$712,843; 1977 — \$785,804; and 1978 — \$417,923.

NOTE D — SALE AND LEASEBACK TRANSACTIONS

During 1973, the Company sold and leased back from outside parties 11 Pizza Hut restaurants and an addition to the home office building. The restaurant leases are for 20 year periods at annual rentals aggregating \$99,998. The lease for the home office addition is for an 18 year period with annual rental of \$34,800. The total sales price of these properties was \$1,245,000 (of which \$525,000 was included in other accounts receivable at March 31, 1973, and was collected by April 6, 1973) and their cost was \$1,239,000. The gain from the sale of these properties has been deferred and will be amortized over the life of the lease.

NOTE E — STOCK OPTIONS

Under the terms of an employee stock option plan, the Company may grant options to officers and employees to purchase shares of its Common Stock at a price not less than the fair market value of the stock at date of grant. Activity under this plan is summarized as follows:

	Number of Shares	Option Price	
		Per Share	Total
Outstanding April 1, 1971	31,520	\$9.38	\$ 295,658
Granted	26,850	9.62 to 20.56	434,111
Cancelled	1,700	9.38	15,946
Exercised	4,088	9.38	38,345
Outstanding March 31, 1972	52,582	9.38 to 20.56	675,478
Granted	27,850	17.13 to 30.00	546,229
Cancelled	4,383	9.38 to 26.81	71,690
Exercised	4,148	9.38	38,908
Outstanding March 31, 1973 (of which 19,811 were exercisable)	71,901	\$9.38 to 30.00	\$1,111,109
Became exercisable in 1972 ..	7,455	\$9.38	\$ 69,928
Became exercisable in 1973 ..	13,188	\$9.38 to 20.56	\$ 167,172

Under the terms of a deferred compensation agreement, a director of the Company will be granted options to acquire shares of the Company's Common Stock at \$6.50 per share. The number of shares covered by these options accumulates until 1976 based on the extent of consulting services rendered by the director. At March 31, 1973, the director was entitled to purchase 2,618 shares under this agreement and approximately \$10,000 annual compensation expense had been charged to income in 1972 and 1973.

At March 31, 1973, Common Stock was reserved as follows:

	Shares
Conversion of 8% convertible notes	26,471
Employee stock option plan	91,764
Warrants to purchase Common Stock at \$9.25 a share	87,500
Options under director's deferred compensation agreement	8,932
	<u>214,667</u>

NOTE F — COMMITMENTS AND CONTINGENT LIABILITIES

The Company and its subsidiaries lease certain land, buildings, and operating equipment for various periods through 2009. These leases require minimum rentals (exclusive of payments for real estate taxes, maintenance, insurance, and excess rentals based on a percentage of unit sales required by some of the leases) in the following periods ending March 31: 1974 — \$6,206,308; 1975 — \$6,108,793; 1976 — \$5,779,515; 1977 — \$5,453,872; 1978 — \$5,308,800; 1979 through 1983 — \$23,392,507; 1984 through 1988

—\$16,750,659; 1989 through 1993—\$7,163,628; thereafter — \$400,890.

At March 31, 1973, as a result of various transactions, the Company was guarantor of lease commitments of certain franchisees. The annual and aggregate commitments under these guarantees is summarized as follows:

Transaction	Annual Commitment	Aggregate Commitment
Guaranteed for a fee	\$414,799	\$ 5,422,127
Minority owned interests	280,150	4,208,111
Resulting from sales to franchisees	193,626	2,406,340
	<u>\$888,575</u>	<u>\$12,036,578</u>

The Company has guaranteed certain obligations of unconsolidated affiliated companies amounting to approximately \$2,000,000.

The Company is a party to pending or threatened lawsuits arising from the normal conduct of its business. While it is not possible to forecast the results of these matters, it is management's opinion that the outcome of these lawsuits will not result in a material adverse effect on the Company's financial position.

NOTE G — SUBSEQUENT EVENTS

Subsequent to March 31, 1973, the Company acquired, in exchange for 96,000 shares of its Common Stock,

23 operating Pizza Huts in transactions which will be treated for accounting purposes as poolings of interests. Upon a consolidated basis, after giving retroactive effect to these acquisitions, the net sales, net income, and net income per share for the years ended March 31, 1973 and 1972, will be as follows:

	March 31	
	1973	1972
Net sales	\$66,903,326	\$48,905,550
Net income	3,531,088	2,096,161
Net income per share:		
Primary	\$1.09	\$.70
Fully diluted	1.08	.70

In April, 1973, the Company completed a loan agreement with an insurance company providing for loans of \$6,000,000 at an interest rate of 9¼%. The Company received \$2,000,000 in April and is committed to borrow the remaining \$4,000,000 by December 30, 1973. These loans are to be repaid in annual installments of \$600,000 beginning in July, 1978.

In May, 1973, the Company sold all the assets, consisting principally of assets relating to the capitalized lease, of its frozen pizza crust manufacturing subsidiary and the purchaser has assumed the related capitalized lease obligation (\$925,000). The operating results of this subsidiary and the loss on the sale were not material.

Accountants' Report

ERNST & ERNST

500 FARMERS & BANKERS BUILDING

WICHITA KANSAS 67202

Stockholders and Board of Directors
Pizza Hut, Inc.
Wichita, Kansas

We have examined the consolidated financial statements of Pizza Hut, Inc. and its subsidiaries for the years ended March 31, 1973, and 1972. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying balance sheets and statements of income, stockholders' equity, and changes in financial position present fairly the consolidated financial position of Pizza Hut, Inc. and its subsidiaries at March 31,

1973 and 1972, and the consolidated results of their operations, changes in stockholders' equity, and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Ernst & Ernst

Wichita, Kansas
May 22, 1973

Officers and Executive Personnel

PRINCIPAL OFFICERS

Frank L. Carney,
President & Chairman of the Board
Robert E. Cressler,
Group Vice President - Operations
James P. Schwartz (deceased, June 16, 1973)
Vice President - Finance
Farris S. Farha,
Vice President - Administration
Robert L. Logsdon,
Vice President - Marketing & Research
Kenneth R. Miller,
Vice President - Pizza Operations
Larry F. Payne,
Vice President - Restaurant Division
John H. Songer,
Vice President - Property Management
M. Hal Taylor, PhD,
Vice President - Distribution & Food Processing
Daniel J. Taylor,
Treasurer & Chief Accounting Officer
Gerald T. Aaron,
Secretary & Counsel

BOARD OF DIRECTORS

Frank L. Carney,
Chairman of the Board & President
Daniel M. Carney,
Investments
G. E. Engleman,
Chairman of the Board, Union Bank of
Ft. Worth and First National Bank,
Hurst, Texas
Martin T. Hart,
Investments
Louis Pozez,
President, Volume Shoe Corporation
James P. Schwartz (deceased, June 16, 1973)
Vice President - Finance
King D. Shwayder
President, Samsonite Corporation

EXECUTIVE PERSONNEL

Accounting
Daniel J. Taylor, Chief Accounting Officer
Max Sutton, Controller
Corporate Information
A. Tracy Burton, Director
Forecasting & Cash Management
David G. Carr, Director
Franchise
Allen L. Brodecker, Director
Human Resources (Personnel)
Stan Sloan, PhD, Director
Legal
Gerald T. Aaron, General Counsel
Albert J. Kirk, Assoc. House Counsel
Management Information Services
Robert J. Navrat, Director
Carl L. Phillips, Manager of Systems & Programming
Philip S. Whiteman, Manager of EDP Operations
Marketing
Sam E. Moyers, Director
Hal W. McCoy, Brand Manager

Office Services

Lois Bird, Director
Pizza Division, Domestic
Kenneth R. Miller, Vice President
Richard M. Bennett, Director of Operations
James E. O'Donnell, Special Assistant to V. P.
H. Roger Karolick, Special Projects Coordinator
Frank Holdraker, Northeast Regional Manager
Hollis Hill, North Central Regional Manager
James Murty, Midwest Regional Manager
Larry L. Strahm, Western Regional Manager
James W. Tucker, Southeast Regional Manager
Ronald G. Williams, South Central Regional Manager
Pizza Division, Foreign
Joseph P. Flynn, Director
Property Management
John H. Songer, Vice President
Gene W. Danitschek, Director of Construction
Kelton Markwell, Director of Excess Properties
Walter E. Murphy, Jr., Director of Development
Public Programs
Herm Bachrodt, Director
Bill Kentling, Director of Information
Research and Development
Stuart T. McCready, PhD, Director
Restaurant Division
Larry F. Payne, Vice President
Specialty Food Division
Gary Moore, Director
Food Service Division
Dave Stwalley, Director
Training
William J. Walsh, Jr., Director

SUBSIDIARIES

Franchise Services, Inc.
Dale E. Wiggins, President
Gary A. Davis, Vice President - Equipment Management
J. Larry Fugate, Vice President - Materials Management
J & G Products, Inc.
William N. Madden, Director

INTERNATIONAL SUBSIDIARIES

Pizza Hut Australia Pty. Ltd.
James McPeak, Managing Director
Jack Kelly, Director of Operations
Pizza Hut (Canada), Ltd.
Randall Ferris, President
Pizza Hut - Costa Rica, Central America
Terry McDonald, President
Pizza Hut, Inc. (English Branch)
Frank Gordon, Managing Director
Ashley Stevens, Director of Operations
Pizza Hut Del Distrito, S.A. de C.V. (Mexico)
Roby Swan, Director
Pizza Hutte, GmbH (West Germany)
Frank Gordon, Managing Director
Stanley T. Ostrowski, Director of Operations

JOINT VENTURE

Pizza Hut Japan, Ltd. (Pizza Hut, Inc. &
Sumitomo Shoji Kaisha, Ltd.)
T. Shinohara, President
Robert Hooper, Director
Sunflower Food Processors, Inc.
Tom Rollert, General Manager

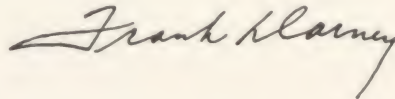
In Memory of
JAMES P. SCHWARTZ

Vice President - Finance

October 9, 1937 — June 16, 1973

His contribution to the favorable financial condition of Pizza Hut, Inc. and the control system he designed will endure to the benefit of the Company.

He was a great personal friend and will be missed.



Joined Pizza Hut, Inc. December 1, 1970

Position Held: Vice President — Finance
Member of Board of Directors

Past Experience: Elmer Fox & Co.—Certified Public Accountant from January 1, 1962 through November 30, 1970.
Staff Accountant from January 1, 1962 through May 31, 1966.
Partner June 1, 1966 through November 30, 1970.

National Director of Management Advisory Services.

Director of MFY Industries, Inc.

Professional Activities:

Member American Society of Certified Public Accountants; Consulting Editor of *Management Services Magazine*.

Education:

Wichita State University — BBA, 1962; Harvard Graduate School of Business — MBA, 1964

Survived by:

Son — James Kendig
Daughter — Tracy Lynn

Pizza Hut,® Inc., 10225 East Kellogg, Wichita, Kansas 67201